Primus' Submission on the ACCC draft report "Pricing Methodology for the GSM Termination Service"

February 2001

Background

In December 2000 the ACCC released a draft report on its proposed pricing methodology for the GSM termination service.

The ACCC has requested comment on the paper. This is Primus' submission to the draft report.

Summary

In summary Primus submits:

- That as a principle, wholesale pricing such as for GSM terminating access (GSM TA) charges, should be based on the underlying costs to provide the service and not retail prices.

- That the most appropriate cost based model for determining wholesale GSM TA pricing is the total service long run incremental cost (TSLRIC) model.

- That the "benchmarking" approach proposed by the Commission is not the most appropriate model for determining GSM TA charges, primarily because

  a) it is not in the interests of end users, and

  b) such an approach as proposed, has inherent fundamental deficiencies.

Primus' Specific Arguments

GSM TA charges should be based upon TSLRIC

Degree of market competition

The Commission's view that a "benchmarking" approach should be adopted is predicated on its belief that the market for wholesale fixed to mobile call charges is a highly competitive one. Primus strongly contends that the wholesale market for fixed to mobile is not highly competitive.

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This indicates that there is little if any incentive for the mobile carriers to offer competitive wholesale GSM TA charges, signifying a relatively weak competitive market.

In a competitive market one would expect to see a reduction in these charges as competition drives charges toward costs.
In deed the Commission's report contains conflicting views about the extent of competition in the market.

Section 7.8 of the report states that TSLRIC pricing would appear to better meet the legislative criteria by ensuring access prices are moved to costs. Primus is in complete agreement with that view. However the report then states that the Commission does not accept that view in the case of the mobile service market and that it prefers a "less intrusive" approach. Primus cannot reconcile the Commission's logic here. Perhaps in a highly competitive market this argument may receive some support. However as the Commission rightly states under section 1.1 of the report *"…the termination element of the mobile services market remains significantly above cost…",* and *"…sustained high access prices for GSM termination appear to be a problem when the service is supplied in relation to fixed to mobile calls…".*

Moreover the Commission itself acknowledges, in section 4.2.4, that *"…it is the Commission's view that the competitive forces in the mobile services market, and in particular on GSM termination will remain relatively weak, now, and in the foreseeable future…"*

Primus contends that these indicators and market dynamics provide more than sufficient justification for proactive intervention rather than a "less intrusive" approach. Without it, fixed line carriers will continue paying inflated termination charges to mobile carriers thereby allowing mobile carriers to subsidise lower customer access prices. Fixed line carrier revenue will be effectively used to increase mobile carrier customer growth.

Retail versus wholesale competition

The report describes in some detail the Commission's view that the retail market for mobile services is a competitive one. To an extent Primus agrees with that. However the report is comparatively short on detail about the competitiveness of the wholesale fixed to mobile segment. This is the segment which should be the focus of the Commission's analysis. Simply because there is competition in the retail market for mobile calls generally does not equate to the existence of a competitive market for retail or wholesale fixed to mobile calls.

Practicality of using TSLRIC

In section 7.1.2 the Commission claims that modeling the mobile network would be problematic and therefore a TSLRIC approach is inappropriate. Primus does not agree. Surely it is more difficult to model the PSTN on TSLRIC given the comparative complexities and the hybrid nature of legacy systems integrated with evolving fixed network technologies. In contrast GSM networks are comparatively the same in terms of network components and should be relatively straightforward to model.

At section 5.2.5 the Commission states that it has limited information regarding the costs associated with providing a mobile call and therefore cannot comment with any certainty on the relativities of retail prices and costs. Primus does not understand why the Commission does not obtain network costing information from the mobile carriers and undertake analysis of termination access costing with the aim at arriving at a cost based wholesale price. In deed Primus strongly recommends that the Commission undertake such an analysis.

The proposed benchmarking approach is inherently deficient

Benchmarking approach is not in the "interests of end users"

About 80% of the total cost of a fixed to mobile call is in interconnect charges. Whilst the mobile carriers can maintain supernormal charges for terminating access, there is no incentive on them to reduce this charge. The benchmark model will provide no incentive for mobile carriers to reduce retail prices as this in turn would erode their ability to reap extravagant profits at the wholesale level. On the other hand a cost based model for wholesale pricing encourages competition at the wholesale level which in turn will contribute to driving down prices at the retail level. This is clearly in the interests of end users.

Further, Primus is unaware of the "benchmarking approach" being used anywhere else in the world, as opposed to cost based approaches which have been widely used. This lack of precedent raises concerns about the viability of a bench marking approach.

Determining the "starting price" is problematic

Primus has real concerns about the Commission's proposal to arrive at the initial wholesale price (the "starting price") by initially setting it at, *"…the lowest current price for the wholesale GSM termination service in the market…."*.

The report provides little reason as to why this is the best approach. The Commission has already identified that current wholesale prices comprise an arbitrage component. Therefore setting the starting price at the lowest wholesale rate is purely arbitrary. There is no basis for this price being considered as an appropriate starting price.

Use of Telstra's Internal Transfer Price

As a general principle, in markets where the incumbent operator has a monopoly over certain services but is also competing in those markets which are open to competition, it is often a requirement that the incumbent provide monopoly services to competitors on the same terms and conditions as it provides them to itself (in terms of supplying competitive services to customers).

Whilst Primus accepts that the market being discussed here (that is, the fixed to mobile market) is not a monopoly market, it does contend that this market exhibits significant bottleneck power. To that extent it would be sensible and reasonable that in attempting to arrive at a wholesale GSM TA charge for non mobile carriers, that an appropriate starting point is the price at which Telstra's mobile business charges its fixed network business for terminating access.

Primus can see no reason why this price in itself could not form the basis of a "cost based" approach to the setting of wholesale prices although it would not account for potential anti competitive cross subsidisation between fixed and mobile businesses within an integrated carrier business such as Telstra's. However, in the event that a benchmark model should be employed, then as a minimum the internal transfer price should be used as the starting price.

Determining the movement in "weighted average retail prices" is problematic

The Commission's draft report omits to explain exactly how it proposes to determine and assess movements in retail prices in order to "peg" the wholesale rate. Primus contends that with the proliferation of retail pricing plans which incorporate varying degrees of handset cross subsidisation, commissions and the like that attempting to arrive at a sensible and meaningful assessment of retail price movement will be practically impossible.

The proposed "monitoring program" will be resource intensive and therefore inefficient

Primus believes that the Commission is already under resourced in the area of telecommunications. Primus is concerned that the Commission's proposed program of monitoring retail prices, the evidence of closed user groups and potential anti competitive pricing on an ongoing basis, will be resource intensive. This will lead to the program becoming unmanageable and ultimately ineffective in ensuring appropriate wholesale pricing.

Basing GSM TA charges upon costs would avoid the Commission having to implement such an onerous regime and lead to a more self regulatory arrangement where access seekers and access providers would have a basis upon which to commercially negotiate pricing.

Other matters

Consumers are ignorant of GSM TA pricing

Primus agrees with the Commission's conclusion at section 4.5 that bottleneck control and consumer ignorance will mean continued high access prices for GSM TA. However Primus does not believe that closed users groups and return calling by mobile customers to fixed line customers is anywhere significant enough to impact GSM TA pricing.

Cross subsidisation

The Commission states in the report that the Part XIB provisions of the Trade Practices Act are open to it to deal with anti competitive cross subsidisation. Primus considers that setting wholesale prices using cost based modelling such as

TSLRIC, would substantially reduce the scope for mobile carriers to cross subsidise, thereby avoiding the Commission having to deal with such anti competitive behaviour.

Primus believes that GSM TA is an access issue and therefore should be dealt with under the access provisions provided in Part XIC. Primus would be concerned if the Commission considers that Part XIB could be used as a surrogate for enforcing the access provisions.